IT 03-0029-GIL 09/02/2003 PUBLIC LAW 86-272/NEXUS

General Information Letter: Nexus determinations are not a proper subject for letter rulings.

September 2, 2003

Dear:

This is in response to your letter dated July 21, 2003 in which you request a letter ruling. The following is in response to your request with respect to Illinois income tax. Your request with respect to sales and use tax has been referred to the Sales Tax Division and will be addressed by a separate ruling. The nature of your request and the information provided with respect to Illinois income tax requires that we respond with a General Information Letter (GIL). A GIL is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code § 1200.120(b) and (c), which may be accessed from the Department's web site at www.ILtax.com.

Your letter states as follows:

> I have been engaged by Company X to review and assist in formulating a voluntary disclosure to bring Company X into compliance with Illinois sales/use and corporate income tax laws. Company X had a change in ownership in 2002, which prompted this review.
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> Company X, a C corporation, was incorporated in June of 1998. It is both incorporated and domiciled in the state of California and is engaged in the development, licensing and maintenance of *state-of-the-art* software application used by healthcare providers; several of such healthcare providers are resident in your state. The company's software products are not sold to individual non-commercial users. Company X has no employees residing in your state and all deliveries into Illinois are through common carrier.
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> Company X is currently a calendar year taxpayer. Prior to the change in ownership, effective January 17, 2002, Company X's fiscal year end was March 31.
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> **Corporate Income Tax:**
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> Heretofore, Company X did not consider its level of its Illinois "in state activity" met the basic threshold requirements for the filing of corporate tax returns. Company X has no payroll, nor employees located in Illinois. Nor does Company X own, lease property, maintain an office or store inventory in the state. However, during the course of this review, Company X has also been advised that the requisite nexus for filing may have been met by Company X's practice of periodic on site visits to their end-user customers typically comprising several days during the course of a nine month installation. Consequently, Company X would like to remedy this situation by proposing the following:
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> 1. Company X will immediately register with the state for corporate income tax purposes and remit any tax due on a prospective basis.
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> 2. Company X will file corporate income/franchise tax returns for the last 3 years. No penalties will be assessed on any taxes owed.
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> 3. If necessary, the Department will verify to its satisfaction, the information contained

on the returns.

4. Company X will not be subject to the payment of penalties (civil or criminal) otherwise assessable for any tax period.

5. The Department will confirm this understanding in writing, provided the information contained herein is accurate.

We appreciate your consideration of the proposed settlement as a means of bringing Company X into compliance with Illinois sales tax and corporate income tax statutes. Company X is not presently undergoing an audit nor has been notified of a pending audit by the Illinois Department of Revenue or any other agency of the state. Nor has Company X filed tax returns in Illinois through a related entity, nor under a different corporate name.

Based on the above, we ask that the Department will accept returns from the company in question for the period beginning July 1, 2003 for sales tax and 4/1/00 for corporate income tax with any tax being remitted for each period plus any applicable interest. Any additional interest that may be due as computed by the Department will be paid when billed. It is requested that these voluntary filings will be accepted by the Department fulfilling any and all past due filing requirements without the application of any penalties or penalty interest.

RULING

Please note that P.A. 93-0026 enacted the Tax Delinquency Amnesty Act. Under this Act, taxpayers that properly remit outstanding tax liabilities will not be assessed interest or penalty with respect to such liabilities. For information on participation in the amnesty program, see Department of Revenue Informational Bulletin FY 2004-11 (August, 2003), which may be accessed from the Department's web site at http://www.revenue.state.il.us/Publications/Bulletins/2004/index.html.

Section 3-10(c) of the Uniform Penalty and Interest Act ("the UPIA"; 35 ILCS 735/3-10(c)) limits the period of assessment in certain cases where a taxpayer voluntarily discloses its failure to file a tax return. The section states:

> In the case of a failure to file a return required by law that is voluntarily disclosed to the Department, in accordance with regulations promulgated by the Department for receiving the voluntary disclosure, the tax may be assessed no more than 4 years after the original due date of each return required to have been disclosed.

The manner in which a taxpayer makes such disclosure is set forth at Regulations section 210.126 (86 Ill. Adm. Code 210.126), which may be accessed from the Department's web site at http://www.revenue.state.il.us/LegalInformation/regs/part210/.

The determination whether a taxpayer has nexus with Illinois is extremely fact-specific. Therefore, the Department does not issue rulings regarding whether a taxpayer has nexus with the State. For information regarding nexus, see Department of Revenue Regulations Section 100.9720 (accessible from the Department's web site). In addition, the following general information may be provided.

The United States Constitution restricts a state's power to subject to income tax foreign corporations and other nonresidents. The Due Process Clause requires that there exist some minimum connection between a state and the person, property, or transaction the state seeks to tax. (*Quill Corp. v. N. Dakota*, 504 U.S. 298 (1992)) Similarly, the Commerce Clause requires that a state's tax be applied only to activities with a substantial nexus to the taxing state. (*Id*.) In the case of foreign corporations, Illinois may assert nexus to tax unless the corporation falls under the protection conferred by Public Law 86-272. (15 U.S.C. § 381) Public Law 86-272 precludes any state from subjecting a nondomiciliary corporation to a net income tax where such corporation's only activities within the state for the taxable year consist of solicitation activities for sales of tangible personal property.

As a general rule, the Department interprets the concept of nexus as broadly as possible. Where any part of a nonresident taxpayer's income is allocable to Illinois under Article 3 of the Illinois Income Tax Act ("IITA" ; 35 ILCS 5/101 *et seq.*), unless protected under P.L. 86-272, the Department will assert jurisdiction to tax.

Section 502(a) of the IITA sets forth the requirements for filing Illinois income tax returns. That section states in pertinent part as follows:

> (a) In general. A return with respect to the taxes imposed by this Act shall be made by every person for any taxable year:
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> (1) For which such person is liable for a tax imposed by this Act, or
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> (2) In the case of a resident or in the case of a corporation which is qualified to do business in this State, for which such person is required to make a federal income tax return, regardless of whether such person is liable for a tax imposed by this Act.

Under this section, a nonresident must file an Illinois income tax return if it incurs a liability for tax imposed under Section 201 of the IITA (or in the case of a corporation qualified to do business in Illinois, if it is required to file a federal return). A nonresident is liable for Illinois income tax under Section 201 if it computes "Illinois net income" as defined under IITA Section 202. IITA Section 202 defines Illinois net income as that portion of the taxpayer's "base income" as defined in Section 203, which is allocated or apportioned to Illinois under the provisions of Article 3 of the IITA, less certain deductions. The above provisions may be accessed from the Department's web site.

IITA Section 304 provides for taxable years ending on or after December 31, 2000 that the apportionment factor for a nonresident deriving business income from Illinois and one or more other states (other than an insurance company, financial organization, or transportation company) shall be equal to its sales factor. Section 304(a)(3)(A) defines the sales factor as a fraction, the numerator of which is the total sales of the person in Illinois during the taxable year, and the denominator of which is the total sales of the person everywhere. Department of Revenue Regulations Section 100.3700(c)(1) states that gross receipts from sales of tangible personal property are allocable to Illinois for sales factor purposes if the property is delivered or shipped to a purchaser within this State, regardless of f.o.b point or other conditions of sale. Regulations Section 100.3370(c)(3) provides that gross receipts from the sale of intangible personal property are allocable to Illinois if the income-producing activity that gave rise to the receipts is performed wholly in Illinois, or the income-producing activity is performed in Illinois based on costs of performance. The above provisions may be accessed from the Department's web site.

As stated above, this is a GIL. A GIL does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you wish to obtain a PLR which will bind the Department, please submit a request conforming to the requirements of 2 Ill. Adm. Code § 1200.110(b).

Sincerely,

Brian L. Stocker
Associate Counsel (Income Tax)